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No. 89-809

In The
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1989

Paine Webber, Inc.,
Kennard L. George and
Dean McGowan,

Petitioners,

vs.

Nancy C. Frye,

Respondent.

RESPONSE TO PETITION FOR A WRIT OF
CERTIORARI TO THE
UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

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RESPONSE TO QUESTION PRESENTED

The Fifth Circuit's decision in Erye v. Paine Webber, et al., 877 F.2d 396 (1989) did not hold that a contractual right to arbitration was waived "merely" by virtue of the failure to file a motion to compel arbitration prior to this Court's decision in Dean Witter Reynolds Inc. v. Byrd, 270 U.S. 213 (1985). Rather, the Fifth Circuit held that the "futility," vel non, of moving to compel arbitration prior to Byrd, standing alone, was not controlling on the issue of whether Petitioners had waived their contractual rights to elect or insist upon arbitration, an issue to be determined on the basis of the totality of the circumstances, Petitioners' affirmative acts and/or inactions, and the prejudice occasioned by Respondent. The Fifth Circuit's decision on the waiver issue in this case simply is not in conflict with the decision of this Court or other Circuit Courts of Appeal.

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Respondent, Nancy C. Frye, Plaintiff below, respectfully files this, its response to petition by Defendants Paine Webber, Inc., Kennard L. George, and Dean McGowan for writ of certiorari to review the opinion of the United States Court of Appeals for the Fifth Circuit, entered on July 18, 1989, which reversed an Order of the United States District Court for the Northern District of Texas, entered on October 14, 1985, and prays that Petitioner's request for said writ be denied or, in the alternative, that this Court, in its wisdom, uphold the correct decision of the Fifth Circuit Court of Appeals.

OPINION BELOW

The opinion of the United States Court of Appeals for the Fifth Circuit is reported at 877 F.2d 396, and is reproduced at Appendix A.

STATEMENT OF THE CASE

In summer, 1982 Nancy C. Frye ("Frye"), Plaintiff-Respondent, opened a securities account with Paine Webber, Jackson, & Curtis, Inc. ("Paine Webber"), entrusting Paine Webber's agents with the protection of her investments. Frye's account, throughout her relationship with Paine Webber, was handled by Paine Webber's employee Ken George and by Paine Webber's Dallas Branch Manager Dean McGowan. Paine Webber and its authorized agents informed Frye that her investments would be managed by means of selling options, a strategy that was to involve the least possible risk to the investor. Trusting their abilities and judgment, Frye signed a Customer's Agreement requiring in part that any dispute arising between Paine Webber and Frye be settled through arbitration.

A dispute arose when, in 1982, Paine Webber lost securities it had invested for Frye. Although Frye and Paine Webber discussed this matter for several months without coming to any satisfactory resolution, Paine Webber failed to notify Frye that it wished to exercise its contractual right to submit the dispute for arbitration. Frye thereupon filed suit on June 16, 1983 in the United States District Court for the Northern District of Texas, Dallas Division, against Paine Webber, McGowan, and George (hereafter collectively referred to as "Paine Webber") as well as Gary Bassett, a private financial advisor, for their breaches of state law and for federal securities violations. Jurisdiction in the Federal District Court was deemed proper.

The case went to trial in February, 1985, more than 19 months after it had originally been filed. In the intervening period of time, Paine Webber participated in extensive litigation, making full use of discovery, asserting counterclaims, and taking part in a trial. As a result of the necessity to respond to Defendant's discovery efforts and to engage in intensive trial preparation, Frye incurred substantial legal and attorney's fees.

The trial proceeded for approximately two weeks in the court of Judge Taylor, until the latter, who suffered from serious illness which eventually led to his unfortunate death, granted a mistrial. The case was then assigned to the Honorable A. Joe Fish for disposition.

Neither during the discussions before Frye filed suit, nor during pretrial discovery or in the course of the trial itself, did Paine Webber engage in any attempt to act upon its contractual right to have the dispute arbitrated by advising Frye of its desire to proceed to arbitration. Paine Webber furthermore did not plead arbitration as an affirmative defense in its answer, nor did it file a Motion to Compel arbitration prior to the mistrial. Paine Webber finally filed a motion to compel Arbitration in October, 1985 — more than 8 months after the aborted trial and 7 months after March 4, 1985, when this Court decided the case of Dean Witter Reynolds Inc. v. Byrd, 470 U.S. 213 (1985).

While this Motion was opposed by Frye, it was erroneously granted by the District Court, which overruled Frye's arguments that Paine Webber had waived its right to arbitration. The district court did not rule as to whether Frye had been severely prejudiced due to: i) the passage of an extended period of time prior to the filing of the Petitioners' motion, ii) the extensive use of judicial discovery procedures, which are not available in arbitration, iii) the time and expense incurred during pretrial proceedings and an aborted trial, and iv) defending against Paine Webber's claims for affirmative relief, including a cross-claim and motion for directed verdict.

Subsequent to arbitration, Frye immediately appealed to the Fifth Circuit Court of Appeals. In reversing the trial court's decision to compel arbitration, the Fifth Circuit Court of Appeals held that Frye had suffered substantial prejudice and that the District Court had erred in not so finding.

REASON FOR NOT GRANTING WRIT

INTRODUCTION

The Petitioners pose their question to this Court as follows:

Should a party to an arbitration agreement be denied its contractual rights merely because it did not file a motion to compel arbitration before this Court decided Dean Witter Reynolds Inc. v. Byrd, 270 U.S. 213 (1985), at a time when such a motion would have been futile?

Premised upon the above-quoted inaccurate characterization of the Fifth Circuit's decision, Petitioners assert that such a holding stands in direct conflict with the decisions of the Eleventh Circuit in Benoay v. Prudential-Bache Securities, Inc., 805 F.2d 1437 (11th Cir. 1986); the First Circuit in Page v. Moseley, Hallgarten, Estabrook & Weeden, Inc., 806 F.2d 294 (1st Cir. 1986); the Ninth Circuit in Conover v. Dean Witter Reynolds, Inc., 837 F.2d 867 (9th Cir. 1987); and the Second Circuit in Rush v. Oppenheimer & Co., 779 F.2d 885 (2nd Cir. 1985).

The Petitioners assert that these other Circuits have held that "any delay or participation in discovery or trial prior to Byrd cannot constitute a basis for a finding of waiver due to the 'futility' of any motion to compel arbitration filed prior to Byrd." Restated, Petitioners take the position that these other Circuits and this Court have heretofore held, contrary to the Fifth Circuit's decision, that Petitioners' right to arbitration did not "arise" or "accrue" until March 4, 1985 — the day Byrd was decided. In the words of Petitioners:

The Fifth Circuit puts litigants in an intolerable position, because Petitioners are held to have forfeited a right they did not have until March 4, 1985. (Emphasis added)

Respondent submits that Petitioners' myopic view of the holding of the Fifth Circuit is inaccurate, and that Petitioners' interpretation of the holdings of the other cited Circuits is equally fallacious. While it is certainly true that other Circuits have taken the view that the filing of a motion to compel prior to the decision in Byrd might have been futile in view of the intertwining doctrine, it simply is not true that any of the other Circuit Courts of Appeal or this Court

has held: (1) that there was no right to elect or invoke a contractual right to arbitration prior to Byrd; (2) that no right to arbitration could have been waived prior to the Byrd decision by the party holding the right through their actions or inactions depending on the stage of the proceeding at which the right is first asserted, any prejudice to the other party occasioned by the delay in assertion of the right, and/or other circumstances relevant to the issue of waiver; or (3) that the traditional and uniformly applied test for waiver of contractual arbitration rights was rendered inapplicable to any securities case decided prior to the announcement of the decision in Byrd. In fact, viewed in proper perspective, Petitioners themselves are seeking to establish a new rule at odds with the holdings of the other Circuits in the cases cited as they attempt to suggest that the case authority in other Circuits have considered the "futility" argument alone in determining whether waiver should or should not be granted. It is Petitioners' misinterpretation of the decisions relied upon which is in conflict with existing authority.

I.

THE FIFTH CIRCUIT DID NOT BASE ITS FINDING OF WAIVER SOLELY ON THE FAILURE OF PAINE WEBBER TO MOVE TO COMPEL ARBITRATION PRIOR TO BYRD

In this instance, the Fifth Circuit determined that despite the strong federal policy favoring arbitration, the right to arbitrate could nevertheless be waived. (Frye, id at P. 399) Miller Brewing Co. v. Fort Worth Distributing Co., Inc., 781 F.2d 494, 497 (5th Cir. 1986); Sedco, Inc. v. Petroleos Mexicanos Mexican Nation Oil Co., 767 F.2d 1140, 1150 (5th Cir. 1985)). Quoting from the decision in Price v. Drexel Burnham Lambert, Inc., 791 F.2d 1156, 1163 (5th Cir. 1986) the Fifth Circuit stated:

. the Arbitration Act had never been intended to abrogate a party's right to arbitration but rather, as this Court noted in Byrd, in enacting the Arbitration Act the purpose of the House of Representatives had been specifically to "place an arbitration agreement 'upon the same footing as other contracts, where it belongs.'" (Byrd, id, at P. 219)

Further, the Federal Arbitration Act, by specifically addressing waiver as one of the defenses as to whether a claim is arbitratable, has recognized that waiver constitutes an inherent recourse in contractual arbitration agreements.

The Petitioners' question, as stated, suggests that the Fifth Circuit's ruling must be interpreted to mean that a party may be found to have waived its right to arbitration solely as a result of having failed, prior to Byrd, to file a motion to compel arbitration. In fact, the Fifth Circuit's decision holds that a failure to assert one's right to arbitration is only one of several factors in addressing the issue of waiver. In examining the lower court's erroneous decision to grant Paine Webber's Motion to Compel arbitration, the Fifth Circuit remarked in Frye, id. at P. 388:

In the instant case, the trial court made no finding as to whether Frye was prejudiced, but held that no waiver had occurred because 'prior to the Byrd decision, a motion to compel arbitration would have been "futile".'

The Fifth Circuit went on to quote Price v. Drexel Burnham Lambert, Inc., 791 F.2d 1156, 1161 (5th Cir. 1986), stating that "we do not accept [the] contention that such a motion would have been futile, and therefore, that a finding of waiver is unjustified in this case" (Frye, id at P. 388); and, in addressing Paine Webber's failure to request arbitration as was its contractual right under the existing agreement, noted:

While the mere failure to assert the right of arbitration does not alone translate into a waiver of that right. . . such failure does bear on the question of prejudice, and may, along with other considerations, require a court to conclude that waiver has occurred. [emphasis added]

In overruling the decision of the lower court in this instance and determining that a waiver had occurred, the Fifth Circuit took into consideration not only Paine Webber's failure to file a motion to compel arbitration, but a number of other factors, not the least of which were Paine Webber's complete neglect in asserting a contractual right to arbitration by informing Frye of its election to arbitrate, Paine Webber's failure at any time to plead a right to arbitration, as a defense or otherwise, filing of the affirmative claims for relief by Paine Webber, and the totality of other circumstances demonstrating

substantive prejudice to Frye. The Fifth Circuit did not base its decision solely on the failure to file a motion to compel arbitration. Rather, it merely rejected the "futility", vel non, of successfully compelling arbitration prior to Byrd as the sole determinant of the waiver issue.

II.

THE FIFTH CIRCUIT APPLIED GENERALLY ACCEPTED STANDARDS DETERMINING WHETHER PREJUDICE SUFFICIENT TO CONSTITUTE WAIVER HAD OCCURRED

In determining whether a court should deny arbitration on the basis of waiver, the party opposing arbitration must show that it will incur substantial prejudice as a consequence. Miller Brewing, Id. at 497; E.C. Ernst, Inc. v. Manhattan Construction Co. of Texas, 559 F.2d 268, 269 (5th Cir. 1977). The courts have generally interpreted the section of the Arbitration Act relevant to waiver to create a heavy burden on the party seeking to claim prejudice. Sibley v. Tandy Corp., 543 F. 2d 540, 542 (5th Cir. 1976) cert. denied; 434 U.S. 824.

More specifically, of the factors which, when found in some combination, may be considered sufficient prejudice to constitute waiver of otherwise arbitratable claims, the courts have over the course of time examined particularly the following: participation in pretrial discovery; failure to plead arbitration as an affirmative defense; forcing the opposing party to respond to motions; forcing the opposing party to respond to a motion for summary judgment; and failure to request arbitration prior to litigation.

In the instant case, the Fifth Circuit, in its deliberations whether Frye had suffered prejudice of sufficient magnitude to deem that Paine Webber had waived its contractual right to arbitration, was faced with a substantial series of prejudicial factors, including:

- (1) the use of the judicial discovery procedures by Paine Webber not available in arbitration;
- (2) the substantial attorney's fees and costs incurred by Frye during both pretrial proceedings and an aborted trial;

- (3) the time and expense of defending against Paine Webber's claims for affirmative relief, including a cross-claim and motion for directed verdict;
- (4) the passage of approximately two-and-a-half years time;
- (5) the complete failure of the Petitioners to ever plead arbitration as an affirmative defense or to ever notify Frye of Paine Webber's election of arbitration;
- (6) the delay of Paine Webber in filing a motion to compel arbitration until October, 1985, approximately 8 months after the aborted trial and approximately 7 months after this Court's decision in Byrd.

Based upon these foregoing considerations, the Fifth Circuit was compelled to find that Frye had suffered prejudiced sufficient to constitute waiver.

III.

THE FIFTH CIRCUIT'S DECISIONS IS IN ACCORDANCE WITH THE DECISION OF OTHER CIRCUIT COURTS OF APPEAL

A number of cases involving less prejudicial factual situations have been selected by Petitioners for the purpose of supporting their contention that the Fifth Circuit decision should be viewed as conflicting with other circuit authority: Benoay v. Prudential-Bache Securities, Inc., 805 F.2d 1437 (11th Cir. 1986); Page v. Moseley, Hallgarten, Estabrook & Weeden, Inc., 806 F.2d 294 (1st Cir. 1986); Conover v. Dean Witter Reynolds, Inc., 837 F.2d 867 (9th Cir. 1987); Rush v. Oppenheimer & Co., 779 F.2d 885 (2nd Cir. 1985). While these cases have evidenced some of the elements determined to be indicative of prejudice, their cumulative effects fell just short of the respective Court of Appeals' tests for waiver, which consequently was not granted.

Petitioners fail to address the numerous other cases where courts have found waiver to exist under facts similar to, albeit less compelling than, those present in this case: E.C. Ernst Inc. v. Manhattan Construction Company of Texas, 551 F.2d 1026, 1040-41(5th Cir. 1977) failure to request arbitration as waiver; Price vs. Drexel Burnham Lambert, Inc., 791 F.2d 1156(5th Cir. 1986); Bengiovi v. Prudential-Bache Securities, Inc., Fed.Sec. L. Rep. (CCH) 92,012 at 91,013 (April 25, 1985) delay 8 1/2 months after complaint had been filed, failure to raise defense of arbitration, participation in discovery, moving for partial summary judgment; Miller Brewing Co. v. Fort Worth Distributing Co. Inc., 781 F. 2d 494, 497 (5th Cir. 1986) waiver will be found when party seeking arbitration substantially invokes the judicial process to the detriment of the other party by demonstrating a clear and unmistakable "disinclination" to arbitrate, including a 3 1/2 year delay, defending against claims, participating in discovery, expending money for legal fees and personal time to prepare, and use of pretrial discovery for arbitration. Further cases where waiver has been found to have occurred under far less prejudicial factual circumstances than exist in the instant case include: Sedco, Inc. v. Petroleos Mexicanos Mexican National Oil Co., 767 F.2d 1140(5th Cir. 1985); Burton Dixie Corp. v. Timothy McCarthy Construction Co., 436 F.2d 405 (5th Cir. 1971); Cornell & Co. v Barber & Ross Co., 360 F.2d 512 (D.C. Cir. 1966); and Fraser v. Merrill Lynch, Pierce, Fenner, & Smith, Inc., 817 F.2d 250 (4th Cir. 1987).

It is respectfully submitted that courts which have found prejudice sufficient to constitute waiver have done so under far less prejudicial circumstances than have confronted Frye. Indeed, the Petitioners would have this Court believe that the subject of participation in a trial as one of the factors comprising prejudice had been deliberated in other Circuit authority and, thus, there is a conflict between these Circuits and the Fifth Circuit's decision in Frye:

The Fifth Circuit's determination that the right to arbitration had been waived due to Paine-Webber's pre-Byrd participation in discovery and trial is in direct conflict with . . . [these decisions]. (Petitioner's Petition for Writ of Certiorari at Page 4, emphasis added)

This claim, however, has no basis in fact. Although the decisions in the cases named above unquestionably set some standards whereby waiver could be determined, none elaborate upon the issue of participating at trial as an element of waiver, as it applies to the Respondent. Indeed, no court has ever directly addressed the issue of prejudice in relation to an aborted trial during which the party seeking prejudice has presented its entire case. We suggest that there can be few additional elements of prejudice not faced by Frye that could potentially be deemed necessary for a finding of waiver. To extend the scope of factors integral to a determination of prejudice sufficient to constitute waiver, moreover, might seriously limit the possibility that any party to a contract could ever waive its contractual rights.

IV.

PETITIONERS' RIGHT TO ARBITRATION AROSE FROM CONTRACT AND DID NOT SPRING FROM THIS COURT'S DECISION IN BYRD

It is not the case that the Petitioners lacked the right to arbitrate before the decisions of Dean Witter Reynolds, Inc. v. Byrd, *supra*, and Shearson/American Express, Inc. v. McMahon, 482 U.S. 220 (1987). The Client Agreement containing the arbitration clause in question affords either party to the agreement the ability to elect arbitration at any time simply by providing written notice to the other party, even while at all times retaining its contractual right to seek or to waive enforcement of arbitration. Burton-Dixie Corporation v. Timothy McCarthy Construction Co., 436 F.2d 405, 407-408 (5th Cir. 1971); E.C. Ernst, Inc. v. City of Tallahassee, 527 F.Supp. 1141, 1142-1143 (N.D. Fla. 1981).

Significantly, Paine Webber did not exercise this option or indicate to Frye that it wished to proceed to arbitration at any point prior to filing its motion to compel after Frye had already been put to the effort and expense of trial. It was in part because the Petitioners had failed to act upon this right granted them by the Client Agreement that the Fifth Circuit noted that it had already overruled the issue of futility in Price, *id.*, at P. 1163, wherein the Fifth Circuit noted that "[the] futility argument assumes that the [other party] would have objected to arbitration had it been raised ab initio." Further, if the

Petitioners had truly wished to protect their right to arbitration, their failure to plead arbitration as an affirmative defense, which had been judicially tested, must also be taken into account.

Thus the Petitioners erroneously claim that their right to arbitration did not accrue until March 4, 1985, when this Court rendered its decision in Byrd, id. By referencing the Federal Arbitration Act as a means to excuse their failure to request arbitration, the Petitioners neglect the fact that arbitration had always constituted an option under the Client Agreement. Moreover, the Arbitration Act was never intended to abrogate a party's right to arbitration but rather, as this Court noted in Byrd, in enacting the Arbitration Act the purpose of the House of Representatives had been specifically to "place an arbitration agreement 'upon the same footing as other contracts, where it belongs.'" (Byrd, id, at P. 219)

Although Byrd leaves little discretion to the trial court other than to compel the enforcement of arbitration agreements, it neither creates the contractual right to arbitration, nor does it remove a person's privilege to waive such a right. What is more, the possibility of waiver is clearly acknowledged in the Federal Arbitration Act. In Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc., 473 U.S. 614, 626(1985), for instance, this Court, citing Moses H. Cone Memorial Hospital v. Mercury Construction Corp., 460 U.S. 1, 24-25 (1983) stated that:

The Arbitration Act establishes that, as a matter of federal law, any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration, whether the problem at hand is the construction of the contract language itself or an allegation of waiver, delay, or a like defense to arbitrability. [emphasis added]

The statute does not preclude the possibility of waiver but merely increases the burden of proof on the party asserting waiver.

The Fifth Circuit expressly recognized the strong federal policy favoring arbitration, as well as the heavy burden on Respondent to prove waiver under the facts presented, but it nevertheless held in favor of Frye based upon application of well recognized waiver principles. In so holding, the Fifth Circuit rejected the lower court's contrary finding based solely on the "futility" argument and

without regard to the prejudice occasioned by Respondent. It did not find a waiver solely due to Petitioners' delay in moving to compel arbitration as urged. The decision of the Fifth Circuit does not represent a conflict of circuits on the same issue, nor does it in any way conflict with any holding of this Court. Rather, it is wholly consistent with decisions of other circuits addressing comparable factual situations. The apparent conflict among the decisions of other courts, therefore, as the Petitioners would have this Court believe, are based upon factual differences between the Petitioners' cases presented and the factual circumstances of the instant case.

CONCLUSION

For these reasons, Respondent requests that the Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit be denied or, in the alternative, that the Fifth Circuit's decision in this case be affirmed.

DATE: February 7, 1990

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CERTIFICATE OF SERVICE

A true and correct copy of this Response has been sent to Petitioner's counsel of record, William D. Sims, Jr. of Jenkins & Gilchrist, P.C. at 1455 Ross Avenue, Suite 3200, Dallas, Texas 75202.

APPENDIX A

FRYE v. PAINE, WEBBER, JACKSON & CURTIS, INC.

Nancy C. FRYE, Plaintiff-Appellant,

v.

PAINE, WEBBER, JACKSON &
CURTIS, INC., etc., et.al.,
Defendants-Appellees.

No. 88-1871.

United States Court of Appeals,
Fifth Circuit.

July 18, 1989

Investor brought action under federal securities law against brokerage firm. The United States District Court for the Northern District of Texas, A. Joe Fish, Jr., granted firm's motion to compel arbitration, denied investor's motion for reconsideration and later confirmed arbitrators' decision to dismiss claim and investor appealed. The Court of Appeals, Patrick E. Higginbotham, Circuit Judge, held that brokerage firm waived contractual right to compel arbitration through participation for approximately two and one-half years in judicial proceedings.

Reversed and remanded.

1. Arbitration 23.25

Trial court's finding that party has waived its right to arbitration is subject to de novo review, but factual findings underlying that conclusion may not be overturned unless clearly erroneous.

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the court.

2. Arbitration 23.3

Despite strong federal policy favoring arbitration, right to arbitrations may be waived.

3. Arbitration 23.4

Both extent of participation by party moving for arbitration in judicial proceedings and delay in moving to compel arbitration are material factors in assessing whether delay was so prejudicial as to constitute waiver of right of arbitration.

4. Exchanges 11(11)

Brokerage firm waived contractual right to arbitration of investor's section 10(b) claim through firm's participation for approximately two and one-half years in judicial proceedings; delay prejudiced investor and furthermore, earlier attempts to compel arbitration would not have been rendered "futile" by doctrine or intertwining which was later rejected in *Byrd*. Securities Exchange Act of 1934, § 10(b), 15 U.S.C.A. § 78j(b).

Appeal from the United States District Court for the Northern District of Texas.

Before JOLLY, HIGGINBOTHAM, and SMITH, Circuit Judges.

PATRICK E. HIGGINBOTHAM, Circuit Judge:

Nancy Frye brought suit against Paine Webber Jackson & Curtis Inc., Dean McGowan, Ken George, and Gary Bassett, asserting federal securities and pendent state law claims. After nearly two-and-a-half years, including extensive discovery and an aborted trial, defendants moved to compel arbitration of Frye's claims. Frye opposed this motion, arguing *inter alia* that defendants had waived their right to seek arbitration by participating in judicial proceedings. The district court granted defendant's motion, holding that any attempt to compel arbitration of Frye's claims before the Supreme Court's rejection of the "intertwining" doctrine in *Dean Witter Reynolds Inc. v. Byrd*, 470 U.S. 213, 105 S.Ct. 1238, 84 L.Ed.2D 158 (1985) would have been "futile." The court denied Frye's motion for

reconsideration and later confirmed the arbitrators' decision to dismiss her claims. We reject the district court's conclusion that the doctrine of intertwining rendered earlier attempts to compel arbitration "futile," and hold that defendants waived their right to arbitration by failing to move to compel arbitration during approximately two-and-a-half years of judicial proceedings. We therefore reverse the district court's decision and remand for trial.

I

Frye opened a securities account with Paine Webber in June 1982, signing an agreement which provided that any controversy between the parties would be settled by arbitration. In June 1983, Frye sued Paine Webber and two of its employees, Ken George and Dean McGowan, claiming that she lost over one million dollars in profits due to mismanagement of her account. She asserted violations of section 10(b) of the Securities and Exchange Act of 1934 and various pendent state law claims. She also brought claims under various provisions of the Securities Act of 1933, which she later voluntarily dismissed.

Despite their agreement to arbitrate, defendants never asserted any right to arbitration. Following over a year-and-a-half of discovery and other pretrial activity, trial commenced before Judge Taylor. At the close of Frye's case-in-chief, Judge Taylor granted the Paine Webber defendants' motion for directed verdict, and the case proceeded against a remaining defendant. Judge Taylor, however, later declared a mistrial and set aside the directed verdict. The case was then transferred to Judge Fish.

In April 1985, defendants demanded arbitration based on the Supreme Court's recent decision in *Dean Witter Reynolds, Inc. v. Byrd*, 470 U.S. 213, 105 S.Ct. 1238, 84 L.Ed.2d 158 (1985) (rejecting doctrine of intertwining and holding that arbitrable pendent claims must be arbitrated). In November 1985, they moved to compel arbitration. Frye opposed the motion, arguing that defendants had waived any right to arbitration by participating fully in discovery and trial without demanding arbitration. The trial court granted defendants' motion, staying all proceedings pending arbitration.¹ The district court ruled that any attempt to compel arbitration of Frye's claims

1. The court stayed Frye's claims against Bassett, which are still pending and are not part of this appeal. The court also stayed Frye's claims against the Paine Webber defendants under Section 12(2) of the Securities Act of 1933. Frye later dismissed those claims voluntarily.

prior to *Byrd* would have been "futile" and that defendants had promptly moved for arbitration after that decision. The court later denied Frye's motion for reconsideration. A panel of arbitrators denied Frye relief. The trial court confirmed the arbitrators' decision and dismissed Frye's claims.

II

On appeal, Frye contends that the trial court erred by compelling arbitration of her claims. She argues that the Paine Webber defendants waived their right to arbitration by their participation in judicial proceedings.

[1, 2] A trial court's finding that a party has waived its right to arbitration is subject to *de novo* review, but the factual findings underlying that conclusion may not be overturned unless clearly erroneous. *Price v. Drexel Burnham Lambert, Inc.* 791 F.2d 1156, 1159 (5th Cir.1986). Despite the strong federal policy favoring arbitration, the right to arbitration may be waived. *Price*, 791 F.2d at 1158 (citing *Miller Brewing Co. v. Fort Worth Distributing Co., Inc. (FWDC)*, 781 F.2d 494, 497 (5th Cir.1986) and *Sedco, Inc. v. Petroleos Mexicanos Mexican National Oil Co. (Pemex)*, 767 F.2d 1140, 1150 (5th Cir.1985). While the party claiming waiver has a heavy burden, " 'waiver will be found when the party seeking arbitration substantially invokes the judicial process to the detriment or prejudice of the other party.' " *Price*, 791 F.2d at 1158 (quoting *Miller Brewing Co.*, 781 F.2d at 497). "Prejudice to the party opposing arbitration, not prejudice to the party seeking arbitration, is determinative of whether a court should deny arbitration on the basis of waiver." *Price*, 791 F.2d at 1162.

In the instant case, the trial court made no findings as to whether Frye was prejudiced, but held that no waiver had occurred because " 'prior to the *Byrd* decision, a motion to compel arbitration would have been 'futile.' " We later rejected this argument in *Price*, 791 F.2d at 1162.

We do not accept Drexel's contention that such a motion would have been futile, and therefore, that a finding of waiver is unjustified in this case. . . . Drexel's argument is undercut by the *Byrd* decision itself, since the decision would never have reached the Supreme Court but for the defendant's insistence on arbitration in the face of the intertwining doctrine. Moreover, Drexel's futility argument

assumes that the Prices would have objected to arbitration had it been raised *ab initio*.

Id. at 1163. *But see Fisher v. A.G. Becker Paribas Inc.*, 791 F.2d 691, 694-97 (9th Cir.1986) (failure to move to compel arbitration during three-and-a-half years of pretrial activity did not constitute waiver since arbitration agreement was unenforceable prior to *Byrd*). The district court erred by finding that the intertwining doctrine rejected in *Byrd* justified defendants' delay in seeking arbitration of Frye's claims.

[3] "While the mere failure to assert the right of arbitration does not alone translate into a waiver of that right ... such failure does bear on the question of prejudice, and may, along with other considerations, require a court to conclude that waiver has occurred." *Price*, 791 F.2d at 1161. Both delay and the extent of the moving party's participation in judicial proceedings are material factors in assessing a plea of prejudice. *id.*

In *Price*, we held that plaintiffs had been sufficiently prejudiced by defendant's seventeen-month delay in seeking arbitration, including the time and expense in responding to discovery and a motion for summary judgment, to conclude that defendants had waived their contractual right to arbitration. *Price*, 791 F.2d at 1160-62.²

See also Fraser v. Merrill Lynch Pierce, Fenner & Smith, Inc., 817 F.2d 250 (4th Cir.1987) (sufficient prejudice to support waiver where brokerage firm delayed four-and-one-half years before seeking arbitration, two trial dates had passed, and opposing party was required to respond to motion for partial summary judgment, and three motions to dismiss). *But see Rush v. Oppenheimer & Co.* 779 F.2d 885 (2d Cir.1985) (insufficient prejudice to support waiver where securities firm delayed eight months in seeking arbitration, filed answer, moved to dismiss claims, and conducted discovery); *Fisher*, 791 F.2d at 698 (insufficient prejudice to support waiver where brokerage firm delayed three-and-a-half years before seeking arbitration, filed pretrial motions, and engaged in extensive discovery); *Page v. Moseley, Hallgarten, Estabrook & Weeden*, 806 F.2d 291

2. The trial court found that Drexel had "initiated extensive discovery, answered twice, filed motions to dismiss and for summary judgment, filed and obtained two extensions of pre-trial deadlines, all without demanding arbitration." The court concluded that the "mounting attorneys fees," "seventeen month delay," and "disclosure which has resulted from the numerous depositions and production of documents" constituted sufficient prejudice to find that Drexel had waived its right to compel arbitration. 791 F.2d at 1159.

(1st Cir.1986) (insufficient prejudice to support waiver where brokerage firm delayed one year before moving to compel arbitration and only prejudice incurred was time and expense of discovery).

[4] Defendants contend that *Price* is distinguishable because Price had been subjected to the burden of defending against a motion for summary judgment before Drexel moved to compel arbitration. Defendants' attempt to distinguish *Price* is unpersuasive, particularly in ignoring the fact that Frye has incurred the time and expense of an aborted trial.

Frye argues that she was prejudiced by (1) defendants' use of judicial discovery procedures not available in arbitration; (2) substantial attorneys' fees and costs incurred during pretrial proceedings and an aborted trial; (3) the time and expense of defending against defendants' claims for affirmative relief, including a cross-claim and a motion for directed verdict; and (4) the passage of approximately two-and-a-half years time. In light of these undisputed facts, we hold that Frye was sufficiently prejudiced by defendants' participation in discovery and trial to conclude that defendants waived their contractual right to arbitration. We therefore reverse the trial court's decision compelling arbitration of Frye's claims and remand for trial.

REVERSED AND REMANDED

